



**DEFENSE CONTRACT AUDIT AGENCY**  
**DEPARTMENT OF DEFENSE**  
8725 JOHN J. KINGMAN ROAD, SUITE 2135  
FORT BELVOIR, VA 22060-6219

IN REPLY REFER TO

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May 9, 2005  
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**MEMORANDUM FOR REGIONAL DIRECTORS, DCAA**  
**DIRECTOR, FIELD DETACHMENT, DCAA**

**SUBJECT: Audit Guidance on Reasonableness and Allowability of Security Clearance  
Bonus/Premium as an Element of Compensation**

In response to recent regional inquiries regarding the allowability of security clearance bonuses and premiums as an element of compensation, we have developed Agency-wide guidance. This memorandum addresses (i) whether bonuses/premiums relative to the recruitment and retention of employees with security clearances are allowable as a compensation element on Government contracts in accordance with FAR 31.205-6, and (ii) the procedures to be used in determining an amount which represents a reasonable bonus/premium for employees with security clearances in accordance with FAR 31.205-6(b).

**GUIDANCE**

*Allowability*

FAR does not specifically state that costs incurred for recruiting and retaining employees with a security clearance are an allowable element of compensation for personal services. However, under FAR 31.205-6(a), compensation for personal services is generally allowable (subject to other provisions in this cost principle), provided it is for work performed by the employee in the current year and does not represent a retroactive adjustment of prior years' salaries or wages. Further, FAR 31.001, Definitions, states:

“Compensation for personal services” means all remuneration paid currently or accrued, in whatever form and whether paid immediately or deferred, for services rendered by employees to the contractor.

Therefore, costs incurred for work performed that are not unallowable in accordance with the FAR cost principles, and are determined to be reasonable and allocable to Government contracts, would be considered allowable compensation costs.

Terms such as premium pay, special pay, and bonuses have been used to describe the additional cost incurred for recruiting and retaining employees with a security clearance. To determine whether these additional payments made to qualified employees are allowable compensation, the nature of the payments must be assessed. Generally, the nature of the remuneration paid represents the higher levels of compensation contractors are being required to pay to recruit and retain individuals who have achieved the level of security clearance required to

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perform on Government contracts. As such, whether labeled as premium, special pay, or bonus, the additional payment is compensation for work performed by the qualified employees and would be allowable compensation for work performed, if reasonable.

Reasonableness

In accordance with FAR 31.201-3, the burden of proof shall be upon the contractor, not the Government, to establish that all compensation, including the premium associated with security clearances, is reasonable. Furthermore, company management is responsible for (i) determining the extent to which external market considerations are used to monitor and influence its pay levels for purposes of ensuring that pay rates are sufficient to attract and retain employees, and (ii) ensure that compensation paid for services rendered on Government contracts is reasonable in accordance with FAR 31.205-6(b)(2).

The guidance in CAM 5-808.9 (“Performance of Audit Procedures to Determine the Reasonableness of Wages and Salaries for Non-Bargaining Unit Employees”) should be followed for determining the reasonableness of the security clearance bonus/premium compensation at a contractor. Specifically,

- A contractor’s adequate compensation system should provide the auditor with sufficient evidence to determine and demonstrate the reasonableness of the security clearance bonus/premium compensation.
- Where the auditor has determined that a contractor’s compensation system does not sufficiently demonstrate that wages and salaries are reasonable in accordance with FAR 31.205-6(b)(2), and the auditor does not have access to pay surveys that adequately represent the contractor’s relevant market, the auditor will refrain from performing an independent test of reasonableness. In this circumstance, the auditor should follow the guidance at CAM 5-808.9(b)(2) and report the condition as a significant system deficiency, and allow the contractor to take corrective action.
- Also, the auditor should coordinate with the ACO to determine if the Government should take any other actions (e.g., contract billing withholds) to protect the Government from being billed for potentially unreasonable compensation costs until the contractor can demonstrate that the additional premium is reasonable.

A consistent following of the above guidance should compel contractors to commission and obtain acceptable compensation surveys to utilize as a basis to demonstrate the reasonableness of the premium paid for employees possessing proper security clearances. Some contractors have been able to demonstrate the reasonableness of the total employee compensation package, including paying premiums for employees with security clearances, by

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using pay surveys that adequately represent their relevant market. Thus, we should expect other contractors, when challenged, to recognize their responsibility to demonstrate the reasonableness of the total employee compensation package and the reasonableness of their security clearance bonus/premium cost in accordance with FAR 31.201-3 and FAR 31.205-6(b).

## **CONCLUDING REMARKS**

Field audit office personnel should refer questions regarding this memorandum to their regional offices. Regions unable to answer, or with questions of their own, should contact the Headquarters, Policy Programs Division, at (703) 767-2270.

/Signed/  
Robert DiMucci  
Assistant Director  
Policy and Plans

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